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Executive Director-Federal Regulatory

EX PARTE ON LATE FILED

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March 21, 1997

Ex Parte

Mr. William F. Caton
Acting Secretary
1919 M Street N.W., Room 222
Federal Communications Commission
Washington, D.C. 20554

RE: Ex Parte Meeting on Universal Service: CC Docket No. 96-45

Dear Mr. Caton:

Yesterday, representatives of BellSouth met with Dr. Joseph Farrell, Chief Economist, Office of Plans and Policy, to discuss BellSouth's position in the above-mentioned proceeding. The attached charts were provided as an aid to the discussion. These charts are consistent with BellSouth's position already filed in this proceeding. Representing BellSouth were Messrs. R. Blau and Peter Martin and the undersigned.

Due to the lateness of the meeting, this notice is being filed on the next business day pursuant to Section 1.1206(a)(2) of the Commission's rules. If you have any questions concerning this filing, please do not hesitate to contact me.

Sincerely,



Maurice P. Talbot, Jr.
Executive Director - Federal Regulatory

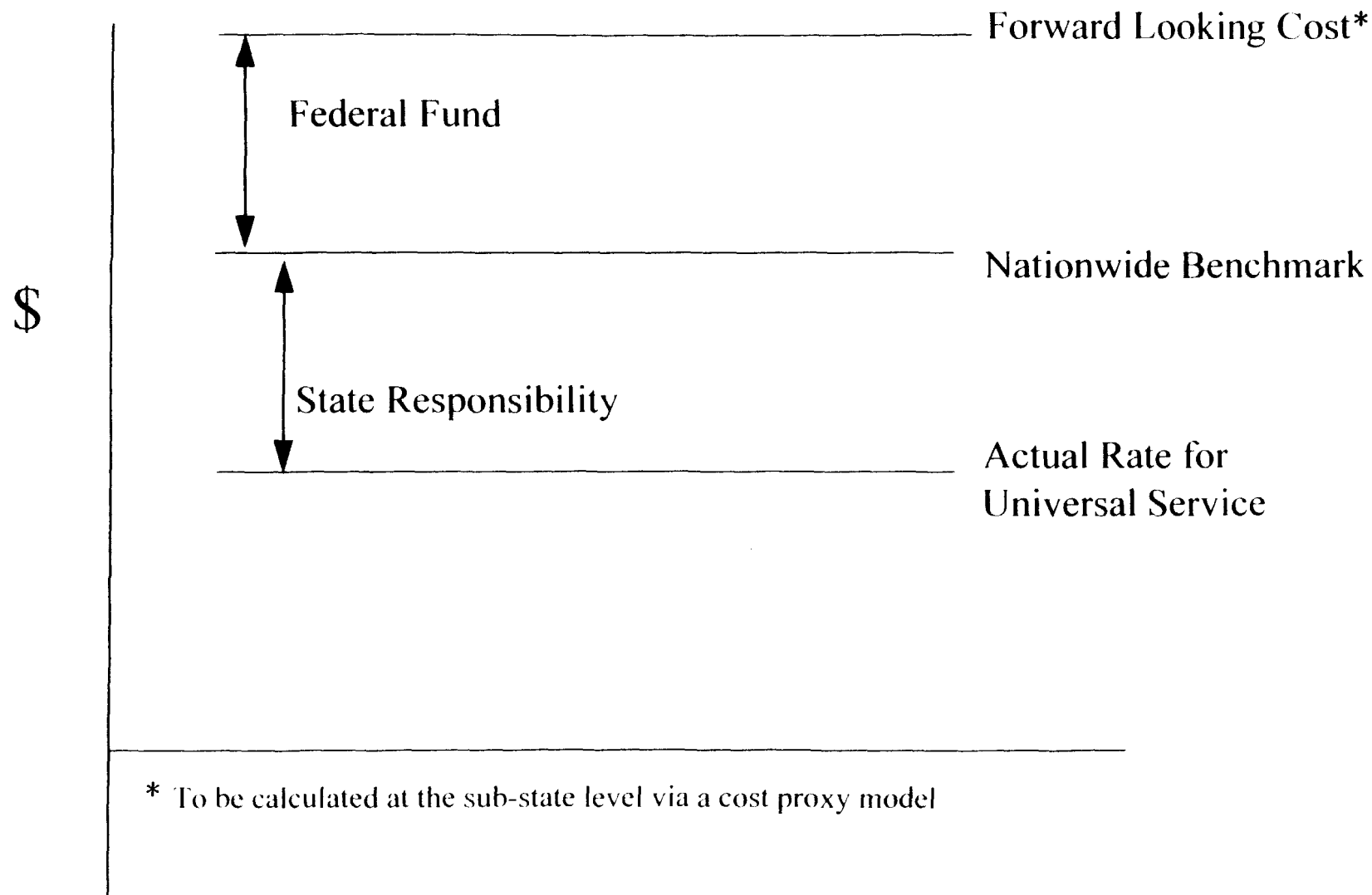
Attachment:

cc: Dr. J. Farrell

UNIVERSAL SERVICE

- Act requires size of fund to be sufficient.
- Act requires that implicit support be made explicit.
- Implicit support is not sustainable in the competitive marketplace.
- Federal sources of implicit support include CCL charge, TIC, and local switching.

UNIVERSAL SERVICE HIGH COST SUPPORT OVERVIEW



For Discussion Purposes

SIZE OF FUND

- Sufficient federal high cost fund (approximately \$8B) would make interstate support explicit.
- Insufficient federal fund burdens high cost states while low cost states pay little or no support.
- Universal Service is premised on low cost areas supporting high cost areas
 - This is not “inequitable”
 - Averages support for high cost and insular areas over large base

FUNDING UNIVERSAL SERVICE

- Funding should be competitively neutral.
- Contributions can and should be based on interstate and intrastate retail revenues.
 - If small fund established, then only interstate revenues should be used.

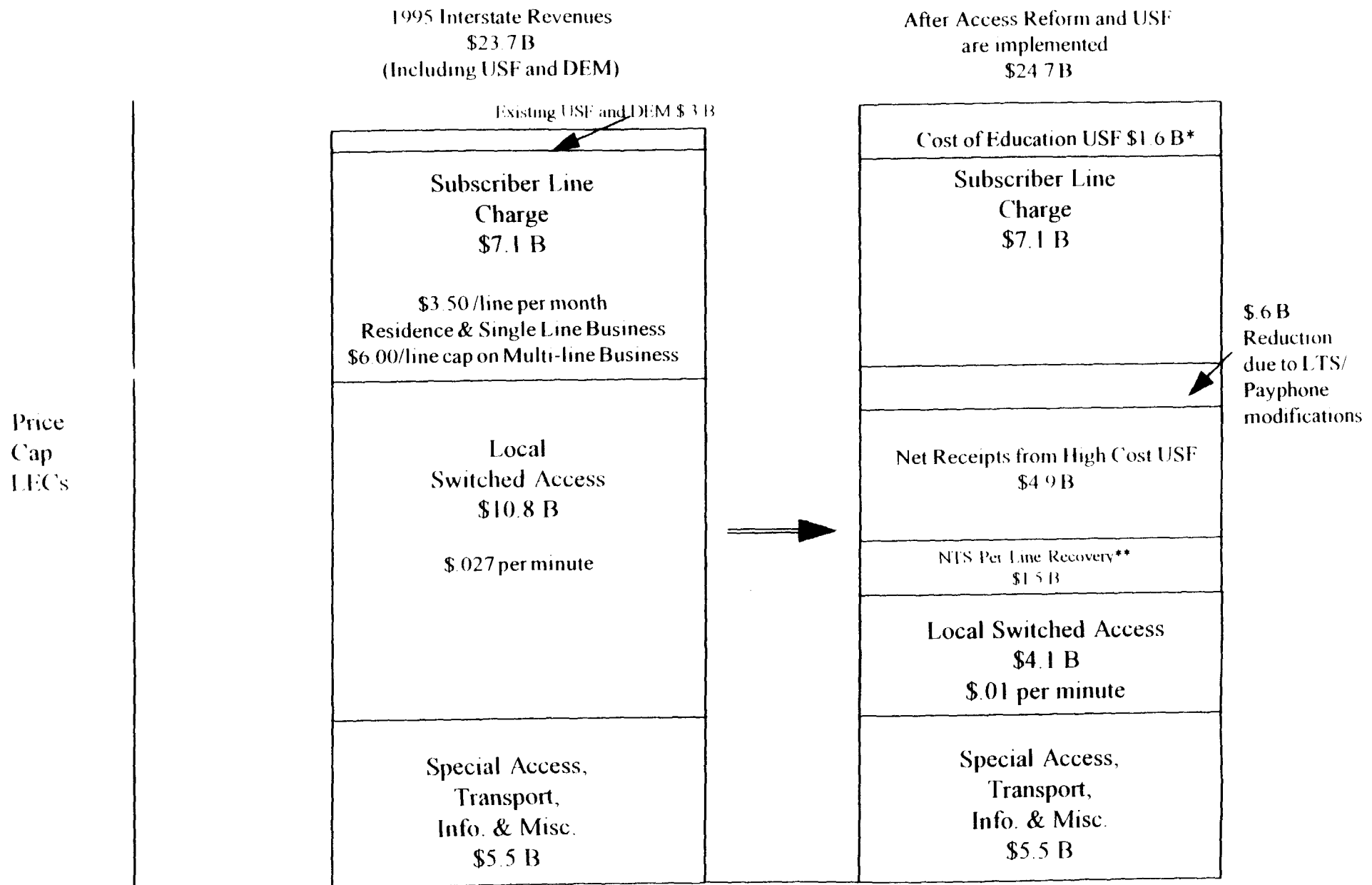
Contributions should be recovered via a mandatory end user surcharge:

- Explicit
 - Competitively neutral
 - Easy to administer.
- Any contributions not recovered by end user surcharge should be recovered from IXCs on flat-rate basis.

UNIVERSAL SERVICE & ACCESS REFORM

- Universal Service cannot be considered in isolation.
- Transforming implicit subsidy to explicit subsidy requires addressing access elements currently under review in Docket 96-262.
- To prevent double recovery, CCLC, TIC and local switching would be reduced based on net receipts from universal service fund.
- If receipts from fund do not cover all of implicit subsidy, then LECs should bill remainder on flat-rate per line basis to IXCs based on number of presubscribed lines.

Access Charge Reform Scenario: Combined State and Interstate USF (\$14.5B)



Notes

1. Does not reflect any modifications to the subscriber line charge
2. \$14.5 B is a conservative estimate of total combined high cost fund (based on BONE)

Based on \$14.5 B Combined Fund (State and Interstate) for High Cost and a \$3 B Fund for Education and Healthcare. Net receipts from Combined High Cost USF (50% of receipts less Interstate assessment) used to recover NIS costs assigned to interstate jurisdiction.

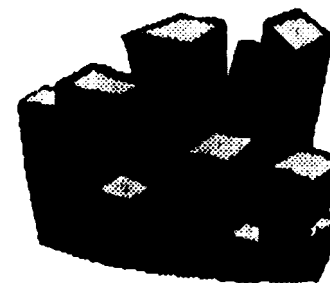
*Method of recovery for Education USF
Surcharge of 1.7% or \$.96 line recovery from all lines

**Method of NIS Per Line Recovery
\$.88 line recovery from all lines

Illustrative - Not to Scale

PERCENTAGE VS. FLAT-RATE SURCHARGE

Percentage of Monthly Billing (4.3%)

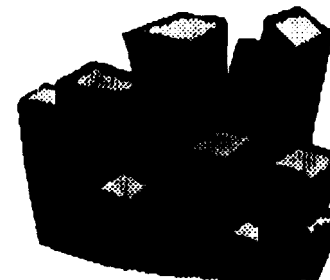


Monthly Bill: \$12
Surcharge% 4.3%
USF Contribution \$0.52

\$30
4.3%
\$1.29

\$200
4.3%
\$8.60

Monthly Flat-Rate Per Line (\$4/Month)



Monthly Bill: \$12
Per Line Charge \$4

\$30
\$4

\$200
\$4

Note: This chart does not reflect the offsetting reductions in toll and other charges which will result
Percentage based on interstate/intrastate revenues, retail revenues approach

Illustrative: For Discussion Purposes Only

A \$10-11 Billion Federal Fund Would Meet “Sufficient” Criteria of the Act

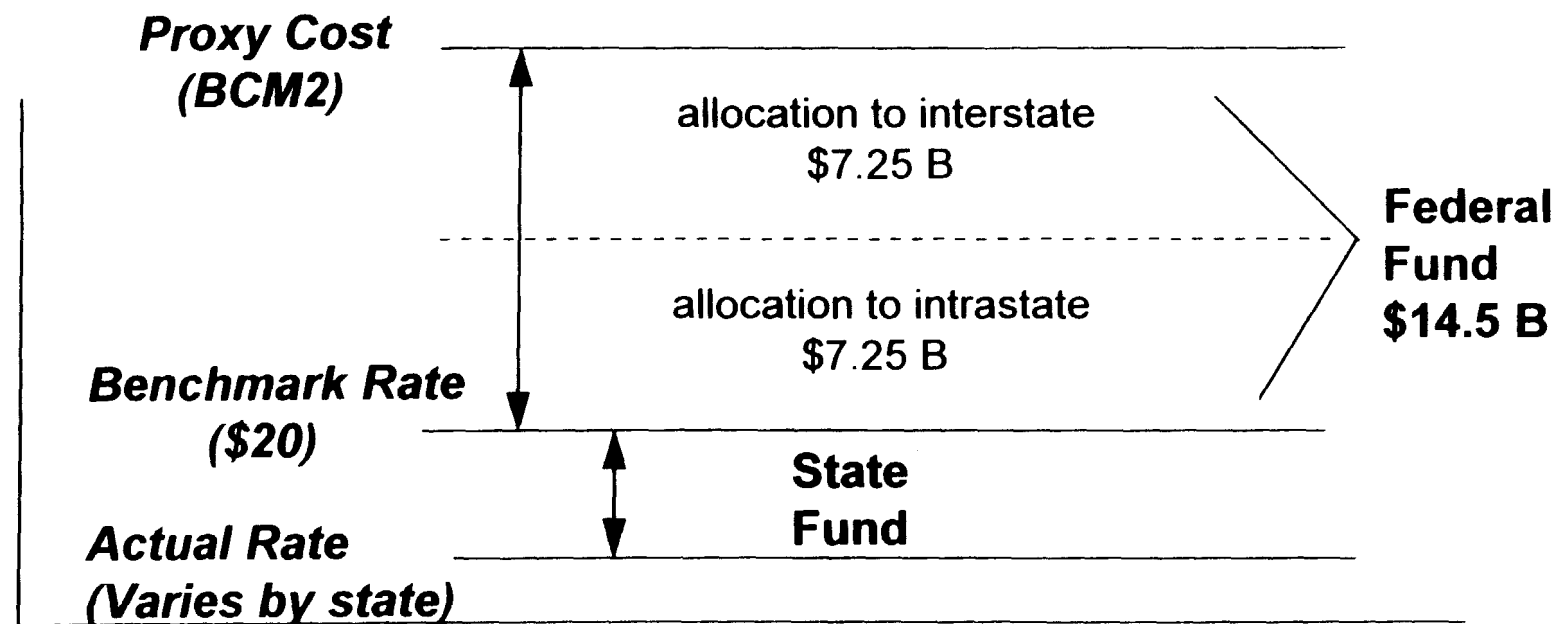
- FCC should take on non-jurisdictional fund which comprises both federal and state.
- \$2.25B for education and libraries and minimal additional funding for health care.
- Lifeline/Link-up programs already in place in most states (\$350M).
- High cost funding based on interstate and intrastate revenues = \$8B.
- Additional implicit support to be dealt with at state level (approximately \$8B).

Another Approach: Allocation of High Cost Fund

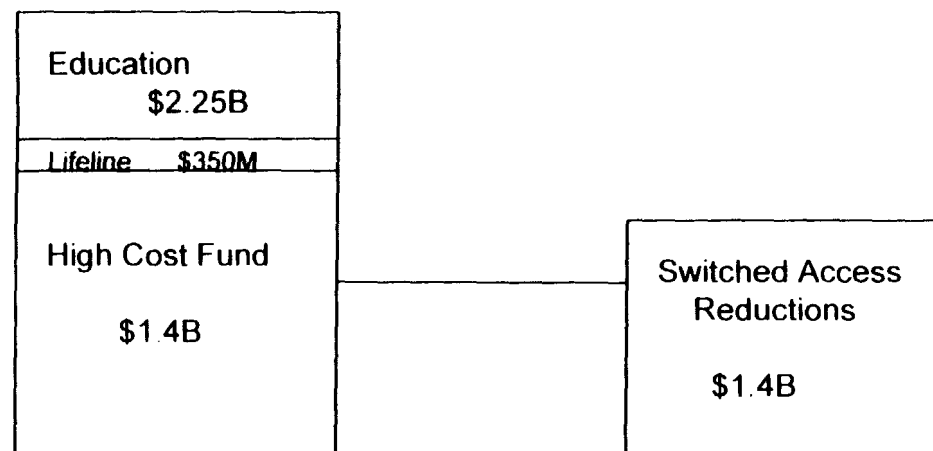
- Fund size should be sufficient to provide needed interstate support.
- Fund could be allocated 50% interstate and 50% intrastate.
- Current HCF precedent in shifting costs to interstate.
- USF used to reduce:
 - Federal
 - State

Switched Access
Switched Access
Toll
Vertical Services
Business Services
- LECs should work with states to determine appropriate offsetting rate reductions. USF should not be used to reduce basic residence or single line business rates.
- A netting approach could be used to assess companies for USF contributions in lieu of an end user surcharge.

EXAMPLE OF UNIVERSAL SERVICE FUNDING SPLIT ALLOCATION APPROACH



A \$4B Interstate Fund Would Not Be Sufficient



- Assessment based on interstate revenues.
- Does not address full amount of implicit subsidy.
- Does not address any of state implicit support (no rate rebalancing).
- Assumes a benchmark at unrealistic \$60.

ADDITIONAL CONCERNS

- Differentiating between primary and secondary residential lines are difficult.
 - Compounded when multiple carrier environment exists.
 - Provides opportunity for arbitrage between providers; one carrier can offer “special deals” to be provider of primary line.
- Primary line identification is also a challenge where customer has multiple dwellings, often in different regions of the country.
- Cost to implement could exceed cost for support of all lines.

PROXY MODEL ANALYSIS

- Original purpose was to identify high cost areas.
- Ideally, actual costs should be used.
However, a reasonable proxy model could suffice.
- Any model used must be carefully designed
 - Build quality realistic network
 - Based on future demand
 - Inputs critical; “garbage in-garbage out”
- Any cost proxy model chosen should be validated against
tops down model (e.g., SPR approach) or actual costs.

CHOICE OF PROXY MODEL

- Ultimate model chosen should be consistent with geographic areas used for unbundled elements to prevent arbitrage.
- All variables that impact costs must be included (e.g., extra costs associated with unique local conditions such as hurricanes or zoning).
- No model currently under review “ready for prime time.”
- Given the importance of model decision, the FCC must continue to work closely with the industry.

Methodology for Implementing a Jurisdictionally Split Federal Fund

- While companies would need to continue to have an opportunity to recover actual costs, the Federal Fund could be based on the results of a reasonable cost proxy model and a nationwide benchmark.
- The Interstate component of the Federal Fund would be calculated by study area. It would equal the interstate CCL, the non-reassigned TIC, the NTS portion of local switching and existing USF and DEM support.
- The Interstate component of funding would be deaveraged based on the results of the cost proxy model.
- The Intrastate component of the Federal Fund would equal the total Federal Fund less the Interstate component of funding.
- LECs would recover their contributions to the Federal Fund via the interstate jurisdiction. Thus, any 'net payer' scenarios would be accommodated via exogenous interstate changes.

Several Approaches for Dealing with a Split Federal Fund

1. Netting Approach Using Combined Revenues
 - Determine by study area each company's net receipts from the federal fund.
 - Make interstate switched access reductions equal to net receipts (up to amount of Interstate support).
 - If additional receipts remain, then make intrastate rate reductions.
2. Netting Approach While Keeping Interstate and Intrastate Components Separate
 - For interstate component, determine net receipts (equal to interstate support less assessment based on interstate revenues).
 - Make interstate rate reductions equal to interstate net receipts.
 - For intrastate component, determine net receipts (equal to intrastate support less assessment based on intrastate revenues).
 - Make intrastate reductions equal to net intrastate support.

Several Approaches for Dealing with a Split Federal Fund (cont'd.)

3. Non Netting Approach

- Determine interstate fund receipts and make corresponding reductions to interstate CCL, TIC and LS.
- Determine intrastate fund receipts (equal to total Federal Fund less interstate support) and let states make corresponding rate reductions.
- Allow LECs to recover their total assessment (based on combined interstate and intrastate revenues) via interstate tariffed charges to IXCs.

BCPM \$20 Fund

RBOC Support Calculations by State - Combined Fund Approach					Netting Approach - Separate Interstate/Intrastate Components					
(\$000,000) and BCPM \$20 Benchmark										
		BCPM	Total	Funded	Payments	Interstate	Funded	Payments	Intrastate	interstate
		Receipts	Interstate	Interstate	Interstate	Rate	Intrastate	Intrastate	Rate	charges to
State	RBOC	\$20 Bchmk	Support	Support	Compon.	Reduction	Support	Compon.	Reduction	fund intrast
Alabama	BellSouth	\$334.3	\$85.5	\$85.5	\$12.5	\$72.9	\$248.8	\$127.8	\$121.0	\$0.0
Alaska	N/A	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0
Arizona	US West	\$260.2	\$102.7	\$102.7	\$15.4	\$87.3	\$157.5	\$122.2	\$35.3	\$0.0
Arkansas	Southwestern	\$203.8	\$29.7	\$29.7	\$5.7	\$24.0	\$174.1	\$58.1	\$116.0	\$0.0
California	Pacific	\$1,182.1	\$342.1	\$342.1	\$91.6	\$250.5	\$840.0	\$897.7	\$0.0	\$57.7
Colorado	US West	\$258.6	\$103.3	\$103.3	\$16.2	\$87.1	\$155.3	\$156.6	\$0.0	\$1.3
Connecticut	SNET	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0
Delaware	Bell Atlantic	\$50.4	\$17.0	\$17.0	\$0.3	\$16.6	\$33.4	\$2.2	\$31.3	\$0.0
Florida	BellSouth	\$544.8	\$260.0	\$260.0	\$38.4	\$221.7	\$284.8	\$334.2	\$0.0	\$49.4
Georgia	BellSouth	\$453.1	\$165.9	\$165.9	\$26.7	\$139.1	\$287.2	\$262.5	\$24.8	\$0.0
Hawaii	GTE	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0
Idaho	US West	\$93.0	\$20.7	\$20.7	\$3.0	\$17.7	\$72.3	\$26.3	\$46.0	\$0.0
Illinois	Ameritech	\$393.3	\$164.3	\$164.3	\$39.2	\$125.0	\$229.0	\$358.4	\$0.0	\$129.4
Indiana	Ameritech	\$245.5	\$54.0	\$54.0	\$13.6	\$40.4	\$191.5	\$121.8	\$69.6	\$0.0
Iowa	US West	\$152.2	\$45.7	\$45.7	\$6.3	\$39.4	\$106.5	\$52.6	\$54.0	\$0.0
Kansas	SBC	\$182.7	\$41.5	\$41.5	\$8.0	\$33.4	\$141.2	\$73.9	\$67.3	\$0.0
Kentucky	BellSouth	\$286.0	\$51.9	\$51.9	\$8.2	\$43.7	\$234.1	\$85.2	\$148.9	\$0.0
Louisiana	BellSouth	\$346.0	\$99.3	\$99.3	\$14.9	\$84.5	\$246.7	\$148.0	\$98.6	\$0.0
Maine	NYNEX	\$138.3	\$34.7	\$34.7	\$3.7	\$31.0	\$103.6	\$46.5	\$57.1	\$0.0
Maryland	Bell Atlantic	\$284.7	\$112.3	\$112.3	\$22.4	\$89.9	\$172.4	\$188.5	\$0.0	\$16.1
Massachusetts	NYNEX	\$350.3	\$225.7	\$225.7	\$27.7	\$198.0	\$124.6	\$286.7	\$0.0	\$162.1
Michigan	Ameritech	\$513.7	\$130.8	\$130.8	\$31.3	\$99.5	\$382.9	\$318.3	\$64.6	\$0.0
Minnesota	US West	\$234.5	\$92.1	\$92.1	\$14.3	\$77.8	\$142.4	\$112.8	\$29.5	\$0.0
Mississippi	BellSouth	\$363.3	\$54.8	\$54.8	\$8.1	\$46.7	\$308.5	\$95.8	\$212.7	\$0.0
Missouri	SBC	\$296.3	\$78.7	\$78.7	\$15.8	\$62.9	\$217.6	\$142.4	\$75.2	\$0.0
Montana	US West	\$72.7	\$14.9	\$14.9	\$2.1	\$12.8	\$57.8	\$21.4	\$36.3	\$0.0
Nebraska	US West	\$81.4	\$23.0	\$23.0	\$3.6	\$19.4	\$58.4	\$39.4	\$19.0	\$0.0
Nevada	Pacific	\$47.2	\$6.4	\$6.4	\$5.9	\$0.4	\$40.8	\$40.0	\$0.8	\$0.0
New Hampshire	NYNEX	\$122.9	\$38.3	\$38.3	\$4.6	\$33.7	\$84.6	\$48.1	\$36.4	\$0.0
New Jersey	Bell Atlantic	\$271.9	\$190.5	\$190.5	\$35.8	\$154.7	\$81.4	\$304.0	\$0.0	\$222.6
New Mexico	US West	\$147.2	\$32.8	\$32.8	\$5.1	\$27.7	\$114.4	\$52.2	\$62.2	\$0.0
New York	NYNEX	\$691.5	\$597.5	\$597.5	\$74.0	\$523.5	\$94.0	\$816.6	\$0.0	\$722.6
North Carolina	BellSouth	\$300.8	\$97.9	\$97.9	\$14.7	\$83.2	\$202.9	\$136.0	\$66.8	\$0.0
North Dakota	US West	\$65.1	\$12.9	\$12.9	\$1.7	\$11.3	\$52.2	\$16.1	\$36.0	\$0.0
Ohio	Ameritech	\$379.6	\$98.6	\$98.6	\$28.4	\$70.2	\$281.0	\$270.2	\$10.8	\$0.0
Oklahoma	SBC	\$264.5	\$50.2	\$50.2	\$9.8	\$40.5	\$214.3	\$91.6	\$122.7	\$0.0
Oregon	US West	\$161.1	\$54.3	\$54.3	\$8.1	\$46.2	\$106.8	\$69.7	\$37.1	\$0.0
Pennsylvania	Bell Atlantic	\$486.9	\$201.8	\$201.8	\$38.2	\$163.5	\$285.1	\$303.5	\$0.0	\$18.3
Rhode Island	NYNEX	\$62.2	\$33.2	\$33.2	\$0.4	\$32.8	\$29.0	\$3.7	\$25.3	\$0.0
South Carolina	BellSouth	\$238.6	\$60.2	\$60.2	\$9.3	\$50.9	\$178.4	\$103.2	\$75.2	\$0.0
South Dakota	US West	\$89.1	\$13.7	\$13.7	\$2.0	\$11.7	\$75.4	\$17.5	\$57.9	\$0.0
Tennessee	BellSouth	\$396.0	\$114.5	\$114.5	\$16.9	\$97.6	\$281.5	\$157.0	\$124.5	\$0.0
Texas	SBC	\$907.0	\$282.3	\$282.3	\$55.2	\$227.1	\$624.7	\$466.0	\$158.7	\$0.0
Utah	US West	\$109.4	\$42.4	\$42.4	\$6.2	\$36.2	\$67.0	\$54.8	\$12.2	\$0.0
Vermont	NYNEX	\$74.0	\$17.2	\$17.2	\$1.9	\$15.4	\$56.8	\$20.0	\$36.8	\$0.0
Virginia	Bell Atlantic	\$332.0	\$106.3	\$106.3	\$21.2	\$85.1	\$225.7	\$175.3	\$50.4	\$0.0
Washington	US West	\$227.7	\$99.8	\$99.8	\$15.0	\$84.8	\$127.9	\$139.3	\$0.0	\$11.4
West Virginia	Bell Atlantic	\$244.4	\$26.4	\$26.4	\$5.1	\$21.3	\$218.0	\$56.7	\$161.3	\$0.0
Wisconsin	Ameritech	\$179.3	\$53.8	\$53.8	\$13.2	\$40.5	\$125.5	\$118.5	\$7.0	\$0.0
Wyoming	US West	\$48.0	\$10.3	\$10.3	\$1.5	\$8.7	\$37.7	\$14.3	\$23.5	\$0.0
Total RBOCs		\$13,167.6	\$4,592.0	\$4,592.0	\$803.4	\$3,788.6	\$8,575.6	\$7,553.6	\$2,412.8	\$1,390.9